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THE MAGAZINE OF REAL ESTATE FINANCE

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MBA at 75: Then, Now and Tomorrow

The Changes in Servicing

Dealing with Overcapacity

1987 Cost Survey

A Plan for the 90s

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OCTOBER 1988 VOLUME 49 NUMBER 1

COVER: MBA's 75th Anniversary

In hindsight, 1914 was a pivotal year. The start of World War I began a chain of events which resulted in a massive impact on American life lasting to this day. It was also the year the Farm Mortgage Bankers Association was born which would evolve into the Mortgage Bankers Association of America. It too would have a significant impact on American life, changing, adjusting and striving for better housing futures. This issue has a brief look back at that important year, and then focuses on the challenges facing MBA members today and tomorrow.

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We Need To Look Back To Look Ahead

Perspective is one of the chief advantages of age. History is an excellent teacher to those who understand the wisdom of learning from past failures and successes.

This month we celebrate 75 years of MBA history, a diamond jubilee. What is there to learn from those early days that's important now? MBA founders had to deal with a complex and rapidly changing culture. With a war about to engulf the world, and with new modes of transportation, society would never be the same. The founders had to deal with these complexities as best they could, all the while accommodating a wide variety of perspectives. The most important lesson is that the founders survived and prospered through teamwork based on knowledge and a code of ethics that said honesty is the best policy.

This month's issue, while celebrating those early days of the Model T, shows we haven't forgotten that fundamental lesson. The major thrust of virtually every article is a tribute to knowledgable teamwork. What our authors implicitly say is here is a creative solution that might help everyone, a solution for servicing, for overcapacity, for affordable housing. It's clear too from the articles on ethics and MBA's new president, Willard Gourley, that we haven't forgotten first principles.

Knowledge, teamwork, honesty. They have brought us a long way since 1914. As we look at the decade ahead in a comprehensive outlook we can be confident that with that past as our guide, we will do well in the future.

Jane DeMarines

Jane DeMarines
Senior Director of Public Affairs
and Marketing

COMING IN NOVEMBER

Going After the Market

When Meredith Willson's Harold Hill was on the train to Gary, Indiana, he told his passengers the simple secret to being a good salesman: "You Gotta Know the Territory." It may be simple, but business pages are filled every day with news of large and small firms who haven't learned this basic lesson. We'll review that basic next month, and show what mortgage bankers are doing once they learn the lyrics.

A special thanks to Rona Mendelsohn for preparing the special report, "A View From the Top" featured in the September issue. Through an editor's error, Ms. Mendelsohn's name was not listed in the credits.

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Evaluating 1987

The MBA cost survey underscores disappointments: some positive movement occurred.

Lyle E. Gramley

In 1987, the mortgage banking industry experienced its most difficult year in recent history. Cyclical and longer-run forces drove costs up sharply, held down the rise of gross income, and sent net income plunging. Overall net income from one- to four-family residential mortgage lending operations was barely above zero for the average firm reporting in the 1987 survey (Chart 1), compared with a typical pre-tax profit margin of 15 to 20 percent during recent years.

Housing finance is a cyclical industry, and mortgage bankers are accustomed to living with adversity. But they were not, and could not have been, fully prepared for the avalanche of problems that hit the industry in 1987. The sources of the difficulties confronted by mortgage bankers were partly cyclical in nature. In particular, the prolonged and deep decline in long-term interest rates that began in the summer of 1984 came to an end in March 1987. The rise in mortgage rates and other long-term securities that occurred thereafter led to the sharpest decline in loan origination volume on record. It also generated huge marketing losses for many firms, although the industry still managed to achieve net marketing profits for the year as a whole.

Some problems facing the industry, however, were longer range in nature. Competition in both loan origination and servicing continues to increase, and mortgage bankers still cannot compete effectively with thrifts in the origination of ARMs. Moreover, the problems plaguing servicing operations in 1986 continued in 1987. Foreclosure losses deepened, while the amortized cost of purchased servicing rose sharply further.

Income from servicing typically has been the mainstay of a residential mortgage banker's income, accounting for between one-third and one-half of gross income from residential mortgage lending operations. Net income from servicing has been the most stable element, as well as the largest, of residential mortgage bankers' pre-tax income.

In 1987, however, the bottom line results for the servicing operation were deeply disappointing (Chart 2). Gross servicing income per loan recorded a significant increase, 8½ percent, but provisions for loan losses, the amortized cost of purchased servicing, and all major elements of direct costs per loan other than personnel expenses rose much faster. As a result, net servicing income fell to $35 per loan, down one fourth from the 1986 level and more than 50 percent below the 1985 level.

In recent years, servicing operations have been plagued with growing problems that have cut deeply into profitability. From 1979 to 1985, net servicing income ranged between .19 and .25 percent of the dollar volume of loans serviced—that is between 19 and 25 basis points—averaging 23 basis points over the seven years (Chart 3). Net income from servicing fell to 11 basis points in 1986 and to 8 basis points in 1987. Virtually all of this squeeze on net income has come from the cost side. Gross servicing income averaged 46 basis points from 1979 through 1985, and was still 43 basis points in 1987. But servicing costs have risen relentlessly, from 21 basis points in 1979 to 35 basis points in 1987. By far the largest part of this increase has occurred within the past two years.

Beginning in 1984, net servicing income per loan began to be held down by larger provisions for loan losses and net losses on foreclosures. Together, these two cost elements reduced net servicing income by $9 per loan in 1984, $12 in 1985, $23 in 1986 and $19 in 1987. Other costs for servicing foreclosures and real estate owned are also increasing. The 1987 survey broke out these costs explicitly; they amounted to over $15 per loan at the average firm reporting in the survey.

Use by the VA of the no-bid option has been a major contributor to increased costs of foreclosures. In fiscal 1986, 15 percent of all VA foreclosures were handled by the no-bid option; this figure rose to 21 percent in fiscal 1987. There is, of course, enormous geographical disparity in both

the incidence of VA foreclosures and the use of the no-bid option. For example, in fiscal 1987, there were only 4 VA loans foreclosed in Boston, and none of these involved use of the no-bid option. In Houston, there were nearly 7,000 VA loans foreclosed, and the no-bid option was employed in a little over 40 percent of the cases.

Servicers with portfolios heavily weighted with loans in the energy-producing regions of the country have suffered a particularly heavy toll of foreclosure costs. Many of them have sought to deal with potential future

CHART 1

Income and Expenses Per Firm (in Thousands) Average Firm, 1985-87

	1987	1986	1985
Gross Income, Total	$26,066	$25,837	$18,156
Loan Production	5,712	5,059	3,042
Warehousing	8,979	9,602	6,545
Marketing	1,770	3,142	1,014
Servicing	9,605	8,035	7,555
Expenses, Total	25,993	20,765	15,515
Loan Production	11,023	8,222	5,849
Warehousing	6,699	6,258	5,033
Marketing	394	313	225
Servicing	7,877	5,972	4,408
Net Income, Total (Before Tax)	73	5,072	2,641
Loan Production	(5,311)	(3,163)	(2,807)
Warehousing	2,280	3,344	1,512
Marketing	1,376	2,829	789
Servicing	1,728	2,063	3,147
Memorandum Items:			
Profit Margin (Before Tax)	0.3%	19.6%	15.5%
Purchased Production as Percent of Total Production	33%	35%	29%
Number of Firms Reporting	124	124	101

CHART 2

Servicing Income and Expenses per Loan Serviced Average Firm, 1985-87

INCOME	1987	1986	1985
Servicing Fees	$177.60	$161.12	$148.38
1st Mortgages	173.92	160.65	148.07
Other Mortgages	3.68	.47	.31
Net Gain (or Loss) on Foreclosures	(5.08)	(10.49)	(6.77)
Other Loan Administration Income	23.29	29.90	29.19
Total Servicing Income	195.82	180.53	170.80
EXPENSES			
Personnel	40.84	37.62	33.58
Loan Administration Employees	33.56	31.25	27.06
Management and Directors	1.11	.21	.23
All Other Personnel	.39	.86	.99
Fringe Benefits	5.63	5.08	5.30
Education and Training	.15	.23	—
Occupancy	5.38	4.58	3.66
Electronic Data Processing	10.14	9.05	6.68
Other Direct Expenses	41.46	31.65	22.11
Equipment Rentals, Excl. EDP	1.57	1.67	1.36
Telephone and Postage	6.57	6.69	6.18
Other Supplies	2.77	2.83	2.39
Travel, Autos, and Advertising	.57	.68	.77
Legal and Auditing	1.01	.91	.79
Expenses to Service Foreclosures and REO	15.14	N/A	N/A
Other Direct Expenses	13.83[1]	18.88	10.62
Total Direct Expenses	97.82	82.90	66.03
Provision for Loan Losses	13.49	12.19	4.98
Amortized Cost of Purchased Servicing	49.39	39.46	23.88
Net Servicing Income (before tax)	35.12	45.99	75.91
Memorandum Items:			
Servicing Profit Margin (before tax)	17.9%	25.5%	44.4%
Servicing Income as Percent of Dollar Volume Serviced	.428	.438	.455
Servicing Fees as Percent of Dollar Volume Serviced	.388	.390	.395
Servicing Expense Ratio[2]	.214	.201	.182
Number of Firms	124	124	101

Only income and expenses that pertain to the day-to-day operation of the servicing operation are included in these figures. Excluded from income are net gains on the sale of servicing rights. Excluded from expenses are items such as amortization of goodwill and of organizational structure that reflect "push down" accounting treatment.

[1] Not comparable with prior years' data.

[2] Total Direct Expenses as a percent of dollar volume serviced.

CHART 3

Trends in Servicing Income and Cost Average Firm, 1979-87

	1979	1980	1981	1982	1983	1984	1985	1986	1987
Percent of Dollar Volume Serviced:									
Gross Income	.45	.46	.45	.46	.44	.47	.46	.44	.43
Expenses	.21	.21	.21	.23	.25	.24	.25	.33	.35
Net Income	.24	.25	.24	.23	.19	.23	.20	.11	.08
Selected Expenses per Loan:									
Provision for Loan Losses	$ .29	$ .48	$ .86	$ (.09)	$ 2.43	$ 4.20	$ 4.98	$12.19	$13.49
Net Losses on Foreclosures	$ .28	$ .16	$ .92	$ 1.11	$ 1.75	$ 4.99	$ 6.77	$10.59	$ 5.00
Amortized Cost of Purchased Servicing	$6.25	$10.25	$10.58	$15.03	$17.88	$20.15	$23.88	$39.46	$49.39

CHART 4

Major Components of Total Servicing Expenses Per Loan

	1983		1987	
	Dollars	Percent of Total	Dollars	Percent of Total
Personnel Expenses	$33.60	40.3	$ 40.84	25.41
Occupancy Expenses	3.48	4.17	5.38	3.34
EDP Expenses	5.69	6.81	10.14	6.31
Other Direct Expenses	20.39	24.41	41.46	25.80
Provision for Loan Losses	2.43	2.91	13.49	8.39
Amortized Cost of Purchased Servicing	17.88	21.41	49.39	30.73
Total	$84.34	100.00	$160.70	100.00

losses from this source by restructuring their portfolios through bulk sales and purchases of servicing.

Increases in the amortized cost of purchased servicing have also been large in the past two years, rising from $24 per loan in 1985 to $39 in 1986, and to $49 in 1987. In both 1986 and 1987, a substantial proportion of the servicing portfolio was lost to refinancings; for servicing purchased earlier, this requires expensing of the unamortized portion of the purchase price. This element of cost was probably also increased in 1987 by sales of servicing rights to improve cash flow and bolster current income. Such sales of servicing rights increase current income at the expense of future income, and are likely to be undertaken only when circumstances require.

Even in earlier years, the amortized cost of purchased servicing per loan had been rising as a result of relatively high market prices for servicing and the increase in purchases of servicing to enlarge the size of servicing portfolios. The increase in servicing portfolios has been quite rapid among survey respondents in recent years; since

CHART 5

Personnel Expenses, 1985-1987

	1987	1986	1985
Number of Loans Serviced per Servicing Employee	570	549	579
Average Salary, Loan Administration Personnel	$18,324	$16,885	$15,187
Total Personnel Expenses per Loan Serviced	$40.84	$37.62	$33.58
Personnel Expense as Percent of Dollar Volume Serviced	.085	.091	.090
Personnel Expense as Percent of Total Direct Servicing Expense	42%	45%	51%
Other Expenses, 1985-1987	**1987**	**1986**	**1985**
Occupancy Expenses per Loan Serviced	$5.38	$4.58	$3.66
Occupancy Expenses per Loan Administration Employee	$2,905	$2,475	$2,053
Occupancy as Percent of Dollar Volume Serviced	.012	.011	.010
EDP Expense per Loan Serviced	$10.14	$9.05	$6.68
EDP Expense per Loan Administration Employee	$5,473	$4,889	$3,747
EDP Expense as Percent of Dollar Volume Service	022	.022	.018
Other Direct Expenses per Loan Serviced	$41.46	$31.65	$22.11
Other Direct Expenses as Percent of Dollar Volume Serviced	.091	.077	.058
Portfolio Dynamics, 1985-1987	**1987**	**1986**	**1985**
Rate of Growth of Dollar Volume Serviced	22.7%	14.4%	15.1%
Rate of Growth of Number of Loans Serviced	11.8%	3.1%	7.0%
Total Servicing Acquisition Ratio* ($)	.70	0.39	0.71
Average Loan Size Serviced	$45,731	$41,263	$37,573
Percent Increase in Average Size Loan Serviced	10.8%	9.8%	10.7%

*The total servicing acquisition ratio is the increase in servicing volume divided by the total of in-house and purchased loan production

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1983, the number of loans serviced by survey respondents has increased by a little over 7 percent a year, while the dollar volume of loans serviced has risen by a bit over 16 percent per year.

The rapid rise of provision for loan losses and the amortized cost of purchased servicing per loan has changed radically the cost structure of the servicing operation during the past few years (see Chart 4). These two cost elements accounted for less than 25 percent of the total in 1983; in 1987 they accounted for nearly 40 percent of the total. By far the largest traditional component of costs, personnel expenses per loan, accounted for 40 percent of the total in 1983 and only 25 percent in 1987.

Some categories of servicing costs are largely beyond the control of the individual mortgage banker. Others, such as personnel expenses per loan, could perhaps be held down by strenuous efforts to improve productivity. Such efforts have met with little success among firms responding to the annual survey of income and expenses. For example, the number of loans serviced per loan administration employee, at 570 in 1987, was about the same as the 591 loans serviced per employee in 1979.

This measure of productivity increased in 1987 from 549 loans per employee in 1986, reflecting a faster growth in the number of loans serviced at the average reporting firm—11.8 percent in 1987 compared with 3.1 percent in 1986. Personnel expenses per loan in 1987, therefore, went up rather moderately 8½ percent, compared with the 18 percent rise in total direct servicing expenses per loan.

Analysis of data submitted in prior years has identified significant scale economies in servicing operations. Returns to scale are less likely to be the dominant influence on profitability in years when elements of expense such as loan losses and the amortized cost of purchased servicing are unusually large, as they were in 1987. Cost economies of large scale operations in servicing, however, are still clearly evident in the 1987 results.

As Chart 6 indicates, the number of loans serviced per servicing employee increases with size; firms with servicing portfolios of less than $500 million serviced 367 loans per employee; those with servicing portfolios in excess of $4 billion serviced 600 loans per employee. Total direct servicing expenditures per loan decline from $120 per loan for the smallest servicers to $96 per loan for the largest. The decline in personnel expenses per loan with increasing size is even more impressive—from $66 per loan for the smallest size group to $37 per loan for

CHART 6

1987 Servicing Income and Expenses per Loan Serviced Grouped by Dollar Volume Serviced

	Less than $500 Million	$500 Million to $1 Billion	$1 Billion to $4 Billion	More than $4 Billion	Average Firm
INCOME					
Servicing Fees	$192.24	$176.51	$171.94	$179.54	$177.60
1st Mortgages	190.48	174.92	168.14	175.61	173.92
Other Mortgages	1.76	1.59	3.18	3.93	3.68
Net Gain (or Loss) on Foreclosures	(9.66)	(4.34)	(2.36)	(6.13)	(5.08)
Other Loan Administration Income	25.86	27.95	23.50	22.69	23.29
Total Servicing Income	208.43	200.12	193.09	196.00	195.82
EXPENSES					
Personnel	66.08	50.38	43.87	37.46	40.84
Loan Administration Employees	55.31	41.27	35.29	31.09	33.56
Management and Directors	3.75	1.24	2.24	0.50	1.11
All Other Personnel	0.25	1.33	0.69	0.16	0.39
Fringe Benefits	6.38	6.27	5.51	5.58	5.63
Education and Training	0.38	0.27	0.13	0.14	0.15
Occupancy	7.62	7.23	6.34	4.68	5.38
Electronic Data Processing	12.99	11.86	9.58	10.07	10.14
Other Direct Expenses	33.73	41.32	37.04	43.68	41.46
Equipment Rentals, Excl. EDP	2.16	2.99	1.81	1.29	1.57
Telephone and Postage	6.17	5.48	6.20	6.87	6.57
Other Supplies	3.81	4.14	3.14	2.42	2.77
Travel, Autos, and Advertising	0.98	0.84	0.69	0.47	0.57
Legal and Auditing	1.28	1.14	1.21	0.90	1.01
Expenses to Service Foreclosures and REO	6.90	12.63	8.75	18.48	15.14
Other Direct Expenses	12.43	14.09	15.25	13.25	13.83
Total Direct Expenses	120.41	110.79	96.84	95.90	97.82
Provision for Loan Losses	3.47	41.47	17.15	9.27	13.49
Amortized Cost of Purchased Servicing	25.60	30.44	30.49	60.51	49.39
Net Servicing Income (before tax)	58.95	17.42	48.61	30.32	35.12
Memorandum Items:					
Number of Loans Serviced Per Servicing Employee	367	463	564	600	570
Average Dollar Volume of Servicing (Millions)	$.218	$.736	$2,027	$8,745	$2,471
Percent Growth, Dollar Volume of Servicing	16.0	12.0	16.6	26.7	22.7
Servicing Acquisition Ratio	0.314	0.364	0.639	1.534	1.044
Number of Firms Reporting	35	28	38	23	124

the largest. The largest firms evidently were well aware of the advantages that size brings, and were seeking to become still larger. Thus, the dollar volume of loans they serviced increased by more than one-fourth during 1987, and their servicing acquisition ratio—the ratio of the increase in their servicing portfolio to the dollar volume of in-house and purchased loan production—was 1.5, well above that of the smaller firms.

The evidence of scale economies in servicing operations also stands out clearly when the reporting firms are grouped by the number of loans serviced per employee (Chart 7). Firms servicing less than 400 loans per employee were comparatively small firms, with average servicing portfolios of less than $500 million. Firms with over 600 loans serviced per employee were comparatively large, with average servicing portfolios of $4.1 billion. The benefits of higher productivity influence cost figures in quite dramatic fashion. Total direct servicing expenditures per loan for the 28 firms with highest productivity are less than half the average for the companies in the lowest productivity group. And this better productivity performance does carry through to the bottom line—firms in the two highest productivity groups earned net income of over $40 per loan serviced, far above the figures for the less productive firms.

Necessarily, 1987 was a year of retrenchment for mortgage banking firms. Staffs were trimmed. Heavy sales of bulk servicing took place to generate cash flow and bolster capital positions. It was a year, also, in which mortgage bankers sought to develop new and more effective business strategies for coping with the environment in which the mortgage banking industry currently operates.

Actually, most firms in the industry entered 1988 leaner and more efficient than they were a year earlier. Fortunately, origination volume at mortgage banking companies picked up a bit early in 1988, as declining mortgage interest rates led to a recovery in new and existing home sales and to a higher proportion of fixed-rate mortgages in conventional lending. These developments are encouraging, and will help the mortgage banking industry to emerge from the deep hole into which it sank in 1987. The task of climbing out of that hole, however, will be long and arduous. **MB**

Lyle E. Gramley is chief economist and senior staff vice president at the Mortgage Bankers Association of America (MBA). Prior to MBA, Mr. Gramley was a member of the Federal Reserve Board and served on the President's Council of Economic Advisors.

CHART 7

1987 Servicing Income and Expenses per Loan Serviced Grouped by Number of Loans Serviced per Servicing Employee

	Less than 400	400 to 500	500 to 600	Greater than 600	Average Firm
INCOME					
Servicing Fees	$202.89	$211.66	$176.80	$155.76	$177.60
1st Mortgages	202.80	203.28	174.72	153.15	173.92
Other Mortgages	0.09	8.39	2.08	2.60	3.68
Net Gain (or Loss) on Foreclosures	(4.03)	(6.97)	(5.61)	(3.64)	(5.08)
Other Loan Administration Income	35.38	18.97	26.07	22.31	23.29
Total Servicing Income	234.24	223.65	197.26	174.42	195.82
EXPENSES					
Personnel	77.33	52.23	41.99	29.47	40.84
Loan Administration Employees	68.72	42.07	34.14	24.48	33.56
Management and Directors	1.51	2.40	1.20	0.23	1.11
All Other Personnel	0.15	0.40	0.37	0.42	0.39
Fringe Benefits	6.62	7.15	6.09	4.27	5.63
Education and Training	0.33	0.21	0.19	0.07	0.15
Occupancy	8.70	[illegible]	4.82	3.46	5.38
Electronic Data Processing	14.97	16.93	10.70	5.22	10.14
Other Direct Expenses	49.35	54.74	42.37	32.17	41.46
Equipment Rentals, Excl. EDP	4.32	2.32	1.32	1.06	1.57
Telephone and Postage	8.21	7.11	6.83	5.88	6.57
Other Supplies	5.11	3.30	2.51	2.43	2.77
Travel, Autos, and Advertising	1.33	0.73	0.58	0.38	0.57
Legal and Auditing	2.60	1.82	0.84	0.51	1.01
Expenses to Service Foreclosures and REO	9.11	23.78	16.41	9.69	15.14
Other Direct Expenses	18.67	15.68	13.87	12.22	13.83
Total Direct Expenses	150.35	132.77	99.88	70.32	97.82
Provision for Loan Losses	59.44	24.58	6.90	7.62	13.49
Amortized Cost of Purchased Servicing	31.09	51.29	41.63	56.47	49.39
Net Servicing Income (before tax)	(6.64)	15.01	48.85	40.01	35.12
Memorandum Items:					
Number of Loans Serviced Per Servicing Employee	314	451	588	754	570
Average Dollar Volume of Servicing (Millions)	415	2,474	3,278	4,128	2,471
Percent Growth, Dollar Volume of Servicing	5.9	19.7	20.3	29.5	22.7
Servicing Acquisition Ratio	0.138	0.796	0.936	1.818	1.044
Number of Firms Reporting	34	33	29	28	124

The boom times began in 1984, and came to an abrupt halt in early 1987. Now serious adjustments are necessary.

Overcapacity

Michael F. Cooper

Overcapacity is obviously having a significant impact on the mortgage banking industry. It's a problem that can be effectively dealt with, but to understand the solutions, a brief review of how the industry found itself in this position is necessary.

Its origin lies in the industry's expansion beginning in 1984. Fueled predominately by pent up demand (and, as yields declined further an overwhelming demand for funds to refinance existing loans) mortgage bankers and institutional lenders began growing. Further, nontraditional companies were attracted by the 28.4 percent returns on average equity produced in 1985. The attraction brought in giants such as Sears, GM, Ford, Prudential and Metropolitan. It is estimated that after-tax profits for newcomers of this size are $10 billion annually with assets of $665 billion, and employing 2.3 million people. Estimates of the total market share goal for these giants equal 45 percent. This burgeoning activity, which came to a halt in April 1987, produced overstaffing, unacceptable levels of fixed overhead, expanded branch systems incapable of producing at acceptable levels, or in other words, overcapacity.

Expense Control: With projected revenues under those of 1986 and 1987, every effort should be made to reduce and monitor fixed and variable expenses without sacrificing market share. The rationale of "If we fund 10 more loans per month in the Portland branch, everything will be okay," could cost a larger portion of future pre-tax income. The graphs depict return on equity (chart 1) and the year-to-year present change in ROE and volume (chart 2). There is little correlation between volume and ROE. Between 1981 and 1982 volume increased 15 percent and ROE increased 80 percent. Between 1984 and 1985, volume increased 25 percent and ROE dropped 20 percent. During the period covered, mortgage bankers produced the greatest ROE in 1983 (22 percent) with less than half the volume of 1986 with a ROE of less than 14 percent in a period of falling interest rates. Controlling the relationship between volume and earnings is a significant management priority in most originations today.

Expense control must begin with the development of expanded reporting capabilities into specific areas. The first is one of work measurement. Each corporate and branch function should be isolated and minimum productivity standards established. For example, minimum productivity standards should be established for loan shipping, loan underwriting, loan closing and loan processing. Once these standards have been established, monthly reports of actual performance can be measured, producing an effective method of managing the work load throughout the corporate facility as well for each individual branch.

The next area of expanded and/or developed reporting capabilities should focus on a basis point expression of the cost for each corporate or branch function in addition to each major category of non-personnel expense such as advertising, stationery, promotional materials, etc.

Utilizing work measurement reports in addition to costs by functional area or category will provide an immediate and clear understanding of the company's overall cost to originate, and provide specific information on areas of increasing expense that need to be addressed.

Looking at charts 3 and 4 during the years of 1983, 1984 and 1985, loan volumes fluctuated approximately 40 percent, from a $50 billion low to a $70 billion high. During the same years, employment grew from 85,000 to 120,000 or 41 percent, ruling out the gain generally realized from the economies of scale. Chart 4 excludes the refinance volume of 1985, 1986 and 1987 and dramatizes the industry's expansion problem: going into the peaks of a volume cycle without regard for the circumstances leading to the high origination levels.

Upgrading staff will lead to a reduction of per unit costs by increasing productivity. Just as rapid expansion produced a dilution in quality production and administrative personnel, overcapacity now provides an opportunity to improve the quality of staff.

Employee compensation based on

ILLUSTRATION BY ANNIE LUNSFORD

volume only should be readdressed to create incentives that produce a high volume of profitable and good quality originations. Unsalable, or worse, repurchased loans, will create two very visible and counter-productive results: large cash losses and a damaged reputation in the secondary market.

Current compensation programs based on pure volume should have two major modifications. These address the industry's inability to control expenses as origination volumes increase, and the substantial growth in quality control problems. The first modification could utilize an expanded capability to monitor expenses. A volume driven compensation program could be amended to allow for a deduction in total compensation income for a branch manager, a regional manager, or a head of production who has allowed expenses to grow beyond an agreed upon unit cost. Since exceptions to underwriting requirements can generally be measured (such as post-closing problems and unusually high delinquencies in segments of a servicing portfolio) the second modification to the compensation agreement could provide for a deduction in overall compensation paid due to poor quality control.

Re-evaluating guidelines established for secondary marketing/risk management may not eliminate losses; however, new guidelines will certainly limit potential losses. Too many companies have managed risk with the 20/20 vision of hindsight rather than establishing guidelines that deal with future levels of involvement and/or minimum requirements for coverage at various levels of risk.

Evaluate all costs of servicing loans. To make ends meet in 1987, a good number of mortgage bankers sold servicing. It may be worthwhile now to evaluate current per loan fees charged by subservicers. When measured against per loan costs in-house, you may find a savings in the use of a subservicer or you may establish the need to finance the purchase of additional servicing to lower unit costs.

Better utilization of today's technology to increase personnel productivity will not only reduce costs, it will increase perceived value in your customer's eyes. The mortgage banking industry has stayed well behind other financial services industries in the development and use of computer systems. Additionally, software providers have focused their attention on one specific area of the origination process and have generally not developed usable programs from the point of origination through servicing. Indeed, some excellent software systems don't even speak to each other, and multiple entries need to be made on multiple systems instead of a unified approach. Compounding this problem are existing systems, including hardware and software, currently in place with large net book values. Unfortunately, the systems and software programs may need to be written off when a company implements a complete systems change.

Overriding the previous issues is a need to provide automated assistance from point of origination through servicing. The ability to take applications in the field which can be down loaded into a processing system and updated as the loan moves from application through underwriting, funding, and ultimately into the servicing system, can increase individual productivity along the origination cycle. Increasing the capacity of each individual involved in origination through servicing may not reduce costs during times of low volume, but it will definitely expand the capability to handle a larger volume with a smaller number of people. Ad-

CHART 1

Mortgage Banking Companies' Earnings

SOURCE: MBA

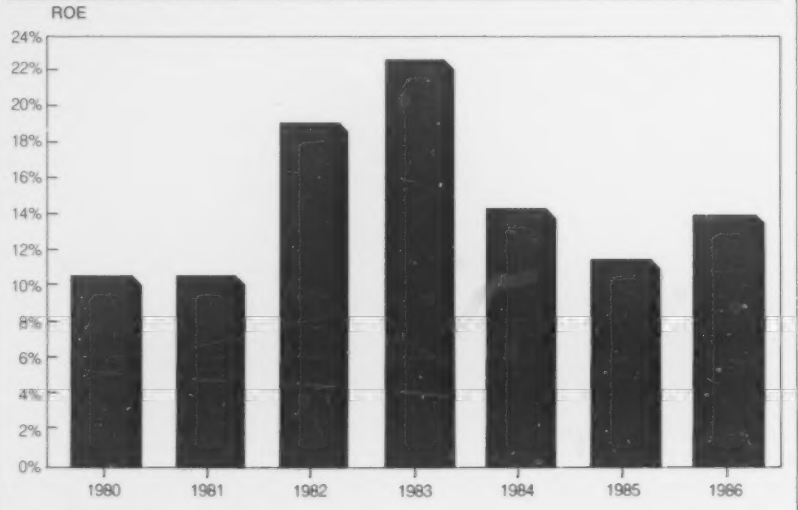
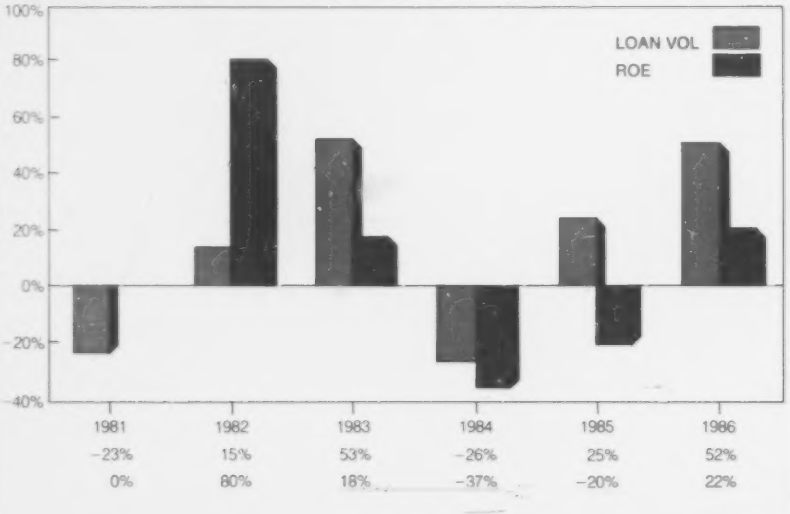


CHART 2

Annual Percent Changes Roe vs. Loan Volume

SOURCE: HUD/MBA



vanced systems and software can definitely assist the industry in moving away from the cycle of expanding overhead as volume increased and frantically scrambling to reduce costs as volume drops. Timely processing of the entire transaction in today's environment of predominately equal products will be the major method of expanding market share in the future.

Year-to-year percentage change in volume and employment are reflected in charts 5 and 6. Once again, growth without regard to operating environment can be seen in most years with or without refinance volume. Between 1983 and 1984 total volume dropped 26 percent and total employment increased 29 percent over the previous year. In 1987, the same attitude is reflected with a 20 percent drop in volume and a 13 percent increase in total mortgage banking staff. Establishing procedures and methods to expand each individual's ability to increase productivity can contribute to the establishment of acceptable relationships between people and volume.

Revisiting 1988's business plan to include strict guidelines for dealing with excessive fixed expenses will assist in the overall cost reduction process. Plans that set in motion predetermined steps to deal with excessive unit costs should be part of future strategic planning.

CHART 3

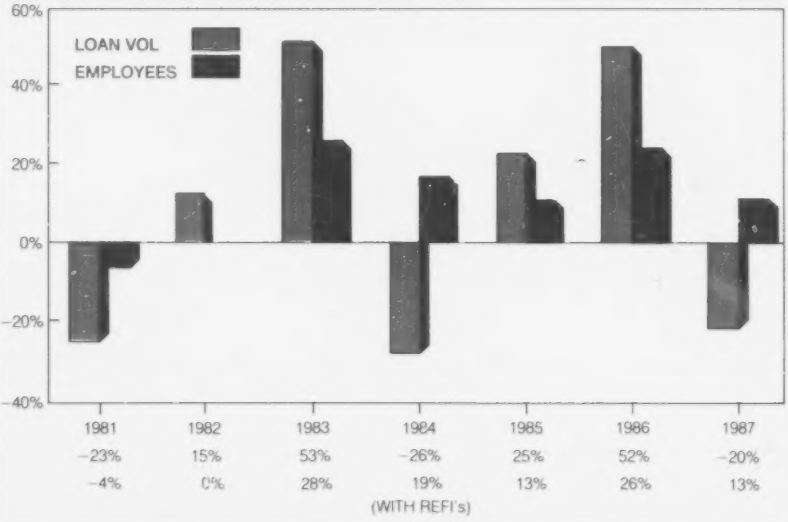
Mortgage Banking Employment vs. Loan Volume

SOURCE: HUD/MBA

CHART 4

Annual Percent Changes, Employment vs. Loan Volume

SOURCE: HUD/MBA



Considering the interest rate volatility that has become a normal part of mortgage banking over the past several years, traditional methods of business planning and financial projecting may not make good business sense for the industry today. The annual establishment of acceptable unit costs could be combined on a quarterly basis with projected volume which would produce a more appropriate management tool for identifying weaknesses in the origination system and produce a more meaningful method of matching overall costs with overall projected income.

Marketing: In some areas of the country, the general reduction of total transactions has been further complicated by portfolio lenders. Portfolio lenders have increased market share by reducing initial yields ½ percent below secondary market requirements. This situation hasn't changed since mid-1987 and will probably continue until we see a further decline in yields for fixed-rate loans. Some mortgage bankers have entered into correspondent relationships with portfolio lenders who provide competitive teaser rates to the branch system which has enabled mortgage bankers to maintain fee income as well as an origination staff. With or without retaining the right to service, the correspondent relationships allow the mortgage banker to maintain control of the transaction from point of origination through funding, unlike brokered relationships that require the underwriting and funding process to take place at the source of funds.

Refocusing the entire origination staff will lead to a larger market share. The origination staff must let go of the hope for a resumption of the refinance business and focus their attention on the 20 percent of the real estate agents that do 80 percent of the transactions. Nontraditional sources of referrals must be identified and marketing strategies need to be developed to reach people such as CPAs, financial planners, business and civic groups, local company relocation staff, financial institutions not providing government financing, for sale by owners, and builders. Regional as well as senior production management must reinvolve themselves in the day-to-day search for a larger market share. A loan officer calling on a builder's subdivision may receive a warm welcome

but no new loans, until a senior person has established a direct relationship between the lender and the builder at the developer's home office.

The marketing strategy necessary to offset the effect of Sears, GM, Ford and the other giants who have entered the industry is quite simple: Provide a higher level of local service responding to the complete need of the local customer.

Prior to 1990, the survivors in mortgage banking will have evaluated their marketing strengths by analyzing each individual branch, looking for the circumstances that surround success or failure. The pattern that develops will usually be created by the people involved and the success of the various products to fill specific market needs. Once a blueprint for success is established, measure all production facilities against this plan. Any weak areas can then easily be addressed and solutions to the problems implemented. The exception to the rule will be the marketing area which does not conform to the established blueprint. Considering the current levels of competition, a change in management, procedures, or the origination staff will most likely not produce a positive effect in a marketing area not suited to your predominant products and services. Closing the office and reinvesting in an area that meets your blueprint specification could be the only solution.

Once you have focused on what you do best and what markets will accept your products and services, maintaining your reputation in a specific market area will require constant attention. Specific needs are constantly changing within any market and you must be prepared to adapt products and services to meet that dominant market's needs. If you take a broad brush approach, the only increase you will have will be the same as everyone else.

Becoming the best local provider of specific services and products will be the key to success in the 1990s. To provide good products and services you must understand your market. In the latter part of 1987, loan agents were complaining about the thrifts' ARM products when in reality Chart 7 indicates that banks increased market share 4 percent while the thrifts stayed even.

Even with the decline in FHA loan volume indicated in chart 8, total fixed- rate volume for 1987 equaled $260 billion (Chart 9—fixed plus Chart 8—government) exceeding all prior years with the exception of 1986. And so, the obvious failure of the mortgage banking industry to monitor the composition of basic volumes by product type allowed a 5 percent loss of market share to the banks.

Training: Effective training programs for all levels of administrative and production employees will lead to increased efficiency and a greater perceived value on the part of your customers.

Over the past few years, the skills of the production staff with respect to basic salesmanship have been dulled by the factors that led to overcapacity. For the sales people that entered the industry in 1985, their view of mortgage banking includes a 40-60 percent refinance customer base. Branch, regional and corporate production management's responsibility in the future will consist of the development of ongoing training programs that refocus or focus (depending on length of employment) the origination staff on sound methods of establishing strong relationships with individuals who can refer business. Training must be developed for the origination staff as they extend into less traditional areas of seeking customer referrals, or in

CHART 5

Annual Percent Changes Employment vs. Loan Volume

SOURCE: HUD/MBA

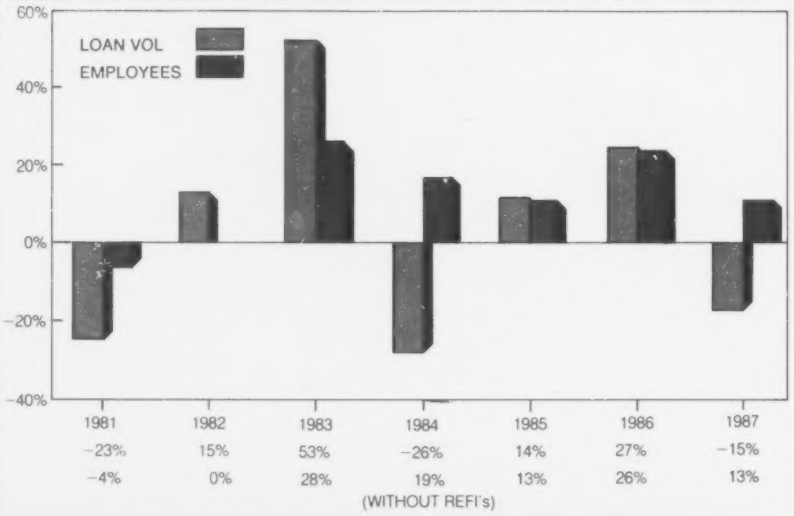


CHART 6

Mortgage Banking Employment vs. Loan Volume

SOURCE: HUD/MBA

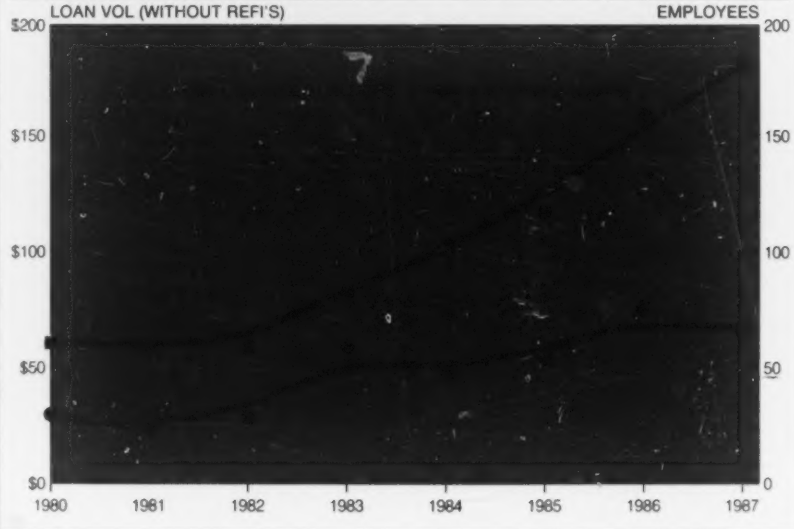


CHART 7

The Market Place

SOURCE: HUD

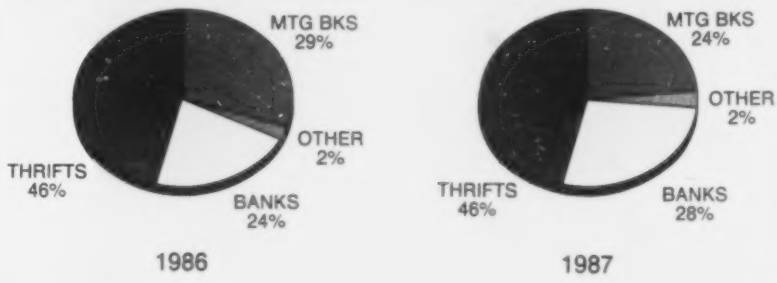


CHART 8

Total Loan Originations

SOURCE: HUD/MBA

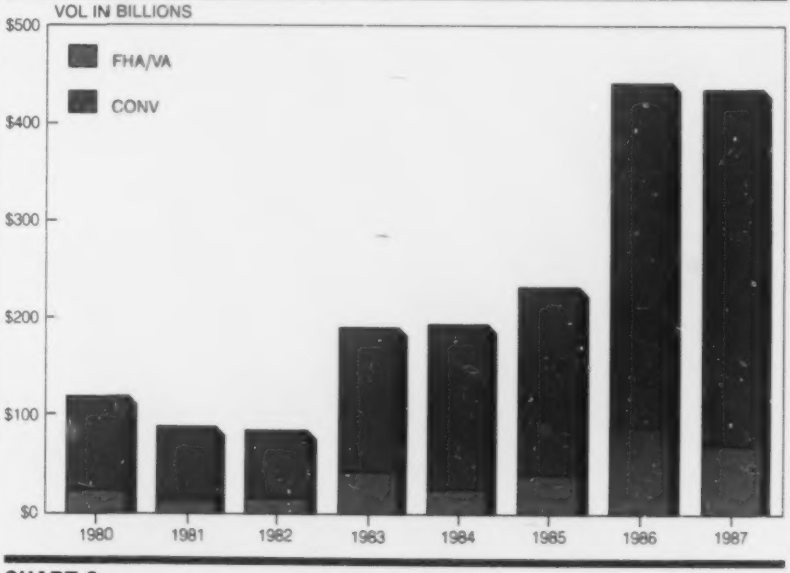
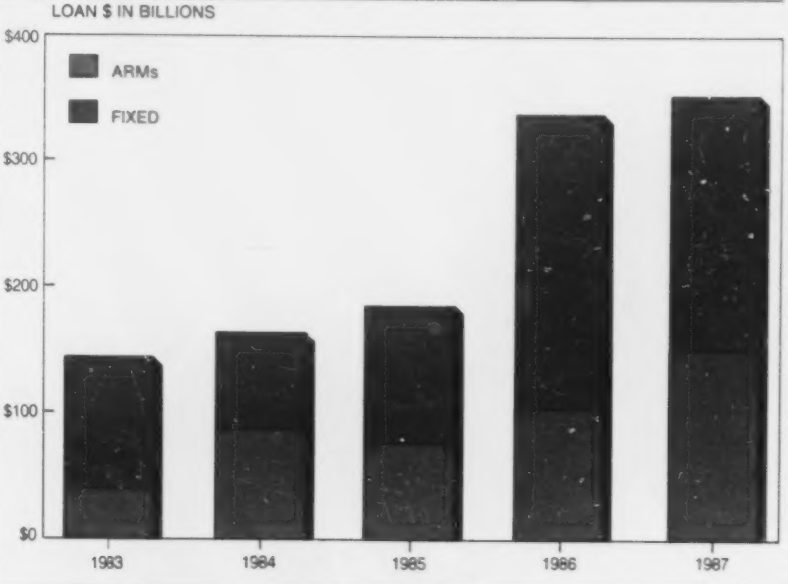


CHART 9

ARMs vs. Total Conventional

SOURCE: HUD/MBA



some cases, direct solicitation. *Sales training from outside sources generally results in short-term increases in productivity if the techniques learned are not incorporated into ongoing training programs.*

The first training program for the administrative staff should address customer service and its impact on perceived value. Just as the loan officers have lost the sharp edge on their sales skills, the administrative staff has relaxed their focus on customer service. Throughout 1986 and until April 1987, it became common practice for the administrative staff to say, "It is just another refinance; I'll deal with it later." The continuance of this mindset will result in a low perceived value on the part of existing customers, and has the potential to undo new relationships established by the sales staff.

The cross-training of administrative staff has historically been the focus of a great deal of conversation and has fallen away with respect to execution in times of high volume. A well executed cross training program will enhance the level of service provided to the consuming public, assist in the reduction of per unit costs, and reduce turnover.

Selective use of outside training programs and seminars will enhance the overall level of knowledge within key areas of the administrative staff. As an example, avoiding a Freddie Mac seminar on underwriting due to costs may result in the inability to sell a percentage of your future production to the agency.

For the near term at least, survival or prosperity for many mortgage executives may well depend upon their ability to effectively manage the change that must take place to cope with overcapacity. Present business plans need to be revised so that executives have the wherewithal to effectively monitor, evaluate and control costs and employee performance. The plan should provide for flexibility so that adjustments can be easily made to capitalize with or cope with changing markets. Finally, initiatives must be undertaken to insure employee productivity and a compensation program suited for our times. **MB**

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With modest rates of appreciation, most homeowners can anticipate a good to excellent return on investment over the years.

THE INVESTMENT RETURNS TO HOMEOWNERSHIP

Richard W. Peach

Roughly two of every three households in this country own the home they live in, and that proportion rises with household income and wealth. Surveys consistently indicate that Americans place homeownership at or near the top of the list of personal priorities. The reasons for this strong preference for owning rather than renting are many. Included among them is the fact that homeownership is regarded as a good investment. Indeed, most households have the bulk of their wealth invested in their home.

It is possible to quantify the expected investment performance of a typical owner-occupied home purchased today, so that the return to homeownership can be compared with returns on other assets, such as stocks or bonds. To do so, a model used to evaluate internal rates of return for income properties was adapted to reflect the tax treatment of homeownership.

For illustrative purposes, the purchase of a $100,000 home at current mortgage interest rates is evaluated, employing realistic assumptions regarding the purchase, operation, and eventual sale of such a property. Table 1 shows estimates of after-tax rates of return on such a purchase with alternative assumptions about the size of the down payment, the rate of home price appreciation, and how long the house is owned. The expected return on the equity in a house is very competitive with rates of return on other assets. For example, if the home appreciates 4 percent per year and is held for 8 years, the annualized after-tax return on equity is about 10 percent, the equivalent of a 12½ percent taxable yield.

The expected return on the equity in a house is very competitive with rates of return on other assets.

Several key underlying assumptions and major findings of this analysis should be specifically addressed.

Rate of Price Appreciation—Given the assumed rate of interest, the rate of price appreciation over the holding period is the key determinant of the return on equity as the capital gain is the major form of return on the investment.

As shown in Table 2, rates of home price appreciation have been lower in recent years than they were earlier—except in the Northeast. A long-run appreciation rate of 4 to 6 percent is probably a realistic assumption, unless a major resurgence of inflation occurs. If that happened, rates on home price appreciation would be higher, but nominal mortgage interest rates would probably also be higher.

Imputed Rental Income—The data in Table 1 include implicit as well as explicit returns to a homeowner. While a homeowner living in his own home does not receive an explicit flow of gross rental income from the property, implicitly he or she receives a flow of income identical to what would be received if the property were rented to someone else. Alternatively viewed, a homeowner avoids the rental payments that would be entailed in living in rental housing. Annual rents, net of utilities, for median priced homes range from about 8 percent to 12 percent of the property value. The exact percentage for a given market area tends to vary inversely with rates of property appreciation. That is, in markets where property values are appreciating rapidly, rents tend to be relatively low as a percent of the property value as investors take a larger portion of their return in the form of capital gain rather than current income. In the analysis underlying the data in Table 1, we have assumed the relationship

TABLE 1

Annualized After-Tax Return on Homeowners Equity

Annual Rate of Appreciation	20 Percent Down payment[a] Holding Period (years)		
	4	8	12
2%	−0.5%	6.4%	8.7%
4%	5.4%	10.1%	11.0%
6%	10.6%	13.4%	13.3%
8%	15.2%	16.3%	15.4%
	10 Percent Down payment[b]		
	4	8	12
2%	−8.6%	4.4%	8.1%
4%	2.3%	10.1%	11.3%
6%	10.6%	14.4%	14.1%
8%	17.4%	18.2%	16.6%

[a] Based on the following assumptions: $100,000 home purchased with an $80,000, 30-year, fixed-rate mortgage with a contract rate of 10 percent plus 2½ points paid in cash. The effective yield assuming a 10 year life is 10.61 percent. Other closing costs equal 0.5 percent of the purchase price, with total equity invested at $22,500. The homebuyer is assumed to have an adjusted gross income of $30,000 and to file a joint tax return with four exemptions. Non-housing itemized deductions are the average for taxpayers at this AGI level. Imputed gross annual rental income as a percent of initial property value, net of utilities, varies with appreciation rate as follows: appreciation rate 2 percent, imputed rental income 9.5 percent; appreciation rate 4 percent, imputed rental income 9.0 percent; appreciation rate 6 percent, imputed rental income 8.5 percent; and appreciation rate 8 percent, imputed rental income 8.0 percent. Annual operating expenses as a percent of initial value are as follows: property taxes, 1.25 percent; property insurance, 0.25 percent; maintenance, 1.5 percent; utilities, 1.5 percent. The underlying inflation rate for income and operating expenses is 4 percent. Expenses of sale are 7 percent of gross sales price.

[b] Same as [a] except that loan amount is $90,000, invested equity is $12,750, adjusted gross income is $34,600 and ¼ percentage point is added to the contract rate of the loan to cover private mortgage insurance.

TABLE 2

Average Annual Rates of Home Price Appreciation

	United States	Northeast	Midwest	South	West
Past 5 Years	4.8%	16.0%	3.7%	3.7%	2.7%
Past 10 Years	7.2%	11.6%	6.0%	7.3%	7.0%
Past 15 Years	8.1%	10.5%	7.0%	7.7%	9.7%

between imputed rental income and property appreciation rates as illustrated in Table 3.

It should also be noted that rents as a percent of property value also tend to decline as one moves above the median home price range. This is due to the fact that demand for rental homes tends to weaken as the price of the home increases.

Holding Period—If sold after one or two years, the rate of return on a home is typically negative since capital gains are insufficient to recoup the upfront costs of the purchase and cover the net operating loss. As the holding period lengthens, the cumulative capital gain surpasses those upfront costs and net operating income increases, causing the rate of return to increase. Eventually, the rate of return will peak and then taper off as equity in the property increases and so leverage decreases. Ultimately, when the loan is fully paid off, the marginal rate of return is the rate of appreciation. How soon the rate of return peaks depends on the rate of appreciation; the faster the appreciation rate the earlier the peak rate of return is achieved. In the case of a 4 percent rate of appreciation, a 10 percent rate of return is achieved in 8 years, but 12 years is required to achieve the peak rate of return of 11 percent. With an 8 percent rate of appreciation the peak is reached in 8 years. As a general rule, when mortgage rates are around 10 percent, rates of price appreciation must be about 5 percent or somewhat higher to make the purchase of a house attractive when the expected holding period is less than about 5 years. Otherwise, an individual may do better by investing the equity in a bond and renting.

TABLE 3

Annual Property Appreciation Rate	2%	4%	6%	8%
Annual Imputed Rental Income, Net of Utilities	9.5%	9.0%	8.5%	8.0%

Tax Treatment—The data in Table 1 assume that the taxpayer faces a 15 percent marginal federal income tax rate and a 5 percent marginal state income tax rate. Homebuyers with sufficient income to be boosted into the 28 or 33 percent marginal federal rates would realize higher rates of return since the relative value of mortgage interest and property tax deductions is greater. Table 1 also assumes that all capital gains are rolled over into another home of equal or higher value and so are not taxed. If capital gains were fully taxed, yield would be reduced about 15 percent when the appreciation rate is 4 percent and about 25 percent when the appreciation rate is 8 percent.

Financing Costs—Obviously, the cost of financing is also a major determinant of yield. The results in Table 1 are based upon a 10 percent contract rate with 2½ points paid in cash. Given rates of home price appreciation, a 1 percentage point higher mortgage interest rate would reduce yield about 30 percent for a 4-year holding period, about 18 percent for an 8-year holding period, and about 13 percent for a 12-year holding period. A 1 percentage point lower mortgage interest rate boosts yields by equal percentages. Not paying points but accepting a higher contract rate, so that the yield to the lender is essentially equal, reduces the peak yield modestly but increases the yield for relatively short holding periods.

This analysis confirms that with relatively modest rates of appreciation homeownership provides very attractive investment returns, which in turn helps explain why people are so eager to become homeowners. But it is also important not to overlook the fact that the returns of homeownership to the individual and to society go well beyond those that can be quantified. **MB**

Richard Peach is deputy chief economist at the Mortgage Bankers Association.

HOUSING ACTIVITY

RESIDENTIAL STRUCTURES, BY UNIT TYPE

(Units in thousands)

YEAR AND MONTH	HOUSING STARTS: Actual Total	HOUSING STARTS: Actual 1-4 Units	HOUSING STARTS: Actual 5+ Units	HOUSING STARTS: Seasonally Adjusted Annual Rates Total	HOUSING STARTS: Seasonally Adjusted Annual Rates 1-4 Units	HOUSING STARTS: Seasonally Adjusted Annual Rates 5+ Units	PERMITS 17,000 ISSUING PLACES: Actual Total	PERMITS 17,000 ISSUING PLACES: Actual 1-4 Units	PERMITS 17,000 ISSUING PLACES: Actual 5+ Units	PERMITS 17,000 ISSUING PLACES: Seasonally Adjusted Annual Rates Total	PERMITS 17,000 ISSUING PLACES: Seasonally Adjusted Annual Rates 1-4 Units	PERMITS 17,000 ISSUING PLACES: Seasonally Adjusted Annual Rates 5+ Units
1988												
FEB	90	68	22	1,519	1,161	358	93	68	25	1,429	1,078	351
MAR	129	105	24	1,529	1,229	300	140	107	33	1,476	1,110	366
APR	154	112	42	1,584	1,151	433	138	101	37	1,449	1,035	414
MAY	140	109	31	1,393	1,056	337	138	106	32	1,436	1,058	378
JUN	149	119	30	1,454	1,149	305	154	114	40	1,493	1,081	412
JUL$_p$	**138**	**106**	**32**	**1,489**	**1,127**	**362**	**121**	**93**	**28**	**1,413**	**1,065**	**348**
1987 TOTAL	1,620	1,211	409				1,535	1,114	421			
1986 TOTAL	1,805	1,263	542				1,770	1,186	584			
7 MONTHS												
1988	878	678	200				854	643	211			
1987	982	742	240				950	698	252			
1986	1,108	772	336				1,070	722	348			
1985	1,016	697	319				1,001	643	358			

RESIDENTIAL STRUCTURES BY REGION

(Units in thousands)

YEAR AND MONTH	HOUSING STARTS: Actual North East	HOUSING STARTS: Actual Mid-West	HOUSING STARTS: Actual South	HOUSING STARTS: Actual West	HOUSING STARTS: Seasonally Adjusted Annual Rates North East	HOUSING STARTS: Seasonally Adjusted Annual Rates Mid-West	HOUSING STARTS: Seasonally Adjusted Annual Rates South	HOUSING STARTS: Seasonally Adjusted Annual Rates West	PERMITS 17,000 ISSUING PLACES: Actual North East	PERMITS 17,000 ISSUING PLACES: Actual Mid-West	PERMITS 17,000 ISSUING PLACES: Actual South	PERMITS 17,000 ISSUING PLACES: Actual West	PERMITS 17,000 ISSUING PLACES: Seasonally Adjusted Annual Rates North East	PERMITS 17,000 ISSUING PLACES: Seasonally Adjusted Annual Rates Mid-West	PERMITS 17,000 ISSUING PLACES: Seasonally Adjusted Annual Rates South	PERMITS 17,000 ISSUING PLACES: Seasonally Adjusted Annual Rates West
1988																
FEB	12	11	42	26	307	259	593	360	13	11	43	26	258	262	553	356
MAR	22	18	53	36	290	262	572	405	26	24	54	37	306	276	525	369
APR	25	32	59	37	265	345	595	379	25	28	48	38	265	272	512	400
MAY	20	30	54	36	200	269	562	362	23	29	49	36	236	274	538	388
JUN	26	32	53	38	240	254	570	380	26	30	57	41	247	282	574	390
JUL$_p$	**25**	**29**	**50**	**35**	**262**	**296**	**563**	**368**	**20**	**24**	**43**	**33**	**222**	**258**	**542**	**391**
1987 TOTAL	269	298	634	420					272	282	575	406				
1986 TOTAL	294	296	733	483					283	290	387	510				
7 MONTHS																
1988	144	159	343	231					144	155	324	232				
1987	157	176	384	264					164	171	359	255				
1986	164	173	470	302					164	167	436	304				
1985	133	133	470	280					146	131	444	281				

HOUSING ACTIVITY (Cont'd.)

YEAR AND MONTH	HOUSING SALES (Units in thousands) EXISTING HOUSES[1] Sold	NEW HOMES Sold	NEW HOMES Available For Sale	NEW HOMES Months Supply at Current Rate	VALUE OF NEW CONSTRUCTION PUT IN PLACE (Dollars in billions) Seasonally Adjusted Annual Rate Total	1 Unit	2+ Units	Non-res.	CONSTRUCTION STATUS (Units in thousands) Seasonally Adjusted Annual Rate Under Construction Total	1-4 Units	5+ Units	Completions Total	1-4 Units	5+ Units
1988														
FEB	220	55	363	6.8	228.5	115.4	22.6	90.5	983	636	347	100	73	27
MAR	303	68	366	6.8	232.9	117.6	21.6	93.7	999	658	341	121	86	35
APR	322	68	362	6.6	232.9	117.4	21.0	94.5	999	661	338	125	86	39
MAY	344	64	367	6.7	234.3	116.2	21.4	96.7	984	647	337	115	88	27
JUN	379	65	365	6.2	231.2	115.1	21.4	94.7	984	651	333	132	100	32
JUL$_p$	**328**	**55**	**366**	**6.6**	**230.4**	**114.4**	**21.8**	**94.2**	**n.a.**	**n.a.**	**n.a.**	**n.a.**	**n.a.**	**n.a.**
1987 TOTAL	3,520	671										1,669	1,194	475
1986 TOTAL	3,565	750										1,756	1,206	550
7 MONTHS														
1988	2,087	418										n.a.	n.a.	n.a.
1987	2,152	432										935	649	286
1986	2,048	487										951	642	309
1985	1,833	416										935	632	303

LENDER ACTIVITY

LONG-TERM MORTGAGE LOANS CLOSED

By Type of Institution and By Unit Type

(Dollars in millions)

YEAR AND MONTH	TOTAL Total	Mtg. Bankers[9]	S&Ls	Banks[2]	Life Cos.	1-4 UNITS Total	Mtg. Bankers[9]	S&Ls	Banks[2]	Life Cos.
1987										
NOV	$ 43,840	$ 5,678	$ 13,708	$ 20,928	$ 3,526	$ 26,482	$ 5,450	$ 11,378	$ 9,432	$ 222
DEC	52,632	6,794	16,617	24,833	4,388	29,464	6,582	12,238	10,530	114
1988										
JAN	36,953	5,919	10,683	18,765	1,586	21,139	5,742	8,327	7,038	32
FEB	35,487	5,886	10,924	17,021	1,656	20,634	5,440	8 507	6,626	61
MAR	42,582	6,878	14,394	19,386	1,924	26,343	6,638	11,575	7,984	146
APR$_p$	**44,028**	**7,000**	**15,228**	**19,972**	**1,828**	**28,022**	**6,702**	**12,668**	**8,547**	**105**
1987 TOTAL	648,148	115,373	210,358	286,789	35,628	445,434	110,093	173,822	158,257	3,262
1986 TOTAL	633,959	142,884	218,118	235,514	37,443	450,232	131,628	176,073	138,717	3,814
4 MONTHS										
1988	159,051	25,683	51,229	75,145	6,994	96,139	24,522	41,077	30,196	344
1987	214,346	49,620	65,389	90,588	8,749	156,988	47,186	54,435	53,980	1,387
1986	135,622	30,266	49,722	47,492	8,142	94,347	28,071	38,765	26,622	889
1985	93,117	17,641	38,764	30,427	6,285	61,067	16,221	28,405	16,192	249

LENDER ACTIVITY (Cont'd.)

LONG-TERM MORTGAGE LOANS CLOSED (Cont'd.)

(Dollars in millions)

YEAR AND MONTH	5+ UNITS				NONRESIDENTIAL			
	Total	Mtg. Bankers[9]	S&Ls	Banks[2]	Life Cos.	Total	Mtg. Bankers[9]	S&Ls	Banks[2]	Life Cos.
1987										
NOV	$ 2,542	$ 151	$ 1,022	$ 983	$ 386	$ 14,609	$ 77	$ 1,308	$ 10,306	$ 2,918
DEC	3,371	97	1,986	969	319	19,797	115	2,393	13,334	3,955
1988										
JAN	2,122	160	1,171	710	81	13,692	17	1,185	11,017	1,473
FEB	2,020	385	990	421	224	12,833	61	1,427	9,974	1,371
MAR	2,387	157	1,349	658	223	13,852	83	1,470	10,744	1,555
APR$_p$	**2,324**	**270**	**1,233**	**656**	**165**	**13,682**	**28**	**1,327**	**10,769**	**1,558**
1987 TOTAL	36,735	2,409	17,719	12,887	3,720	165,979	2,871	18,817	115,645	28,646
1986 TOTAL	40,449	7,172	19,877	9,677	3,723	143,278	4,084	22,168	87,120	29,906
4 MONTHS										
1988	8,853	972	4,743	2,445	693	54,059	189	5,409	42,504	5,957
1987	12,160	882	5,320	5,111	847	45,198	1,552	5,634	31,497	6,515
1986	9,073	1,113	4,879	2,112	969	32,202	1,082	6,078	18,758	6,284
1985	7,026	758	3,999	1,712	557	25,024	662	6,360	12,523	5,479

LONG-TERM COMMITMENT ACTIVITY

By Type of Institution

(Dollars in millions)

YEAR AND MONTH	ISSUED DURING MONTH					OUTSTANDING				
	Total	Mtg. Bankers[9]	S&Ls	Banks[2]	Life Cos.	Total	Mtg. Bankers[9]	S&Ls	Banks[2]	Life Cos.
1987										
NOV	$ 29,450	$ 4,604	$ 15,454	$ 6,636	$ 2,756	$126,075	$12,484	$47,784	$49,673	$16,134
DEC	26,649	2,907	15,561	6,170	2,011	111,370	6,711	44,927	46,613	13,119
1988										
JAN	28,343	7,271	13,929	5,618	1,525	106,598	8,111	41,990	43,325	13,172
FEB	27,456	4,490	13,525	6,598	2,843	110,839	9,147	43,049	44,404	14,239
MAR	37,497	3,969	18,742	10,858	3,928	117,502	7,453	45,589	48,532	15,928
APR$_p$	**36,479**	**3,569**	**19,895**	**9,421**	**3,594**	**126,301**	**7,972**	**47,067**	**54,091**	**17,171**
1987 TOTAL	475,252	96,534	235,457	110,306	32,955					
1986 TOTAL	532,999	128,480	231,915	133,504	39,100					
4 MONTHS										
1988	129,718	19,299	66,091	32,495	11,833					
1987	167,313	41,310	78,289	37,023	10,691					
1986	148,517	43,030	66,430	25,611	13,446					
1985	91,326	14,018	48,881	18,801	9,626					

MORTGAGE INSURANCE

(Units in thousands, Dollars in millions)

YEAR AND MONTH	APPLICATIONS RECEIVED (Units)				LOANS INSURED							
	Total	FHA[3]	VA	Private	Total		FHA		VA		Private	
					Units	Amt.	Units	Amt.	Units	Amt.	Units	Amt.
1988												
FEB	139	84	17	38	103	7,271	56	3,351	20	1,503	27	2,417
MAR	175	109	15	51	98	7,036	49	2,927	19	1,381	30	2,728
APR	165	93	14	58	88	6,591	42	2,508	14	1,039	32	3,044
MAY	170	91	18	61	113	8,222	59	3,545	16	1,164	38	3,513
JUN	168	85	20	63	111	8,466	50	3,006	16	1,209	45	4,251
JUL$_p$	**147**	**74**	**18**	**55**	**130**	**9,565**	**72**	**4,383**	**17**	**1,287**	**41**	**3,895**
1987 TOTAL	2,341	1,211	409	721	2,278	159,373	1,315	81,553	452	33,315	511	44,505
1986 TOTAL	3,279	1,907	450	922	1,853	127,758	921	56,901	346	24,719	586	46,138
7 MONTHS												
1988	964	537	102	325	643	47,123	328	19,720	102	7,583	213	19,820
1987	1,657	908	290	459	1,476	102,609	862	53,575	307	22,430	307	26,604
1986	1,251	475	240	536	919	63,169	446	27,508	162	11,549	311	24,112
1985	960	215	126	619	711	46,206	198	11,376	93	6,293	420	28,537

SECONDARY MARKET ACTIVITY

(Dollars in millions)

YEAR AND MONTH	FNMA Portfolio Comm.	FNMA Portfolio Purc.	FNMA Mortgage-Backed Securities Outstanding	FNMA Mortgage-Backed Securities Issued	FHLMC* Comm. to Sell	FHLMC* Comm. to Buy	FHLMC* Mtg. Purc.	FHLMC* Mtg. Sold	GNMA Pass-Through Securities Applications	GNMA Pass-Through Securities Issued
1988										
FEB	$ 2,516	$ 2,629	$142,797	$ 3,190	$ 1,869	$ 4,911	$ 3,293	$ 2,414	$ 3,694	$ 3,142
MAR	3,823	2,776	145,242	3,352	2,973	4,262	2,932	2,312	3,458	3,106
APR	2,555	2,409	149,569	5,444	2,968	6,437	2,772	2,266	4,820	3,315
MAY	2,142	2,138	152,826	4,600	3,552	5,159	2,876	2,325	6,288	4,168
JUN	2,179	2,372	157,438	6,220	4,288	6,447	4,117	3,649	n.a.	n.a.
JUL$_p$	**1,108**	**1,960**	**160,636**	**4,895**	**n.a.**	**n.a.**	**n.a.**	**n.a.**	**n.a.**	**n.a.**
1987 TOTAL	25,415	20,531	—	63,230	68,210	76,615	76,840	75,018	116,611	96,983
1986 TOTAL	32,987	30,826	—	60,566	106,563	136,179	103,474	102,443	152,911	98,169
7 MONTHS										
1988	14,323	14,284	—	27,701	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
1987	13,717	10,853	—	42,254	52,841	57,466	58,194	57,085	83,414	67,400
1986	19,441	13,709	—	29,465	54,004	57,159	47,797	45,694	72,846	46,539
1985	12,002	12,798	—	9,726	24,834	27,611	23,200	21,403	33,225	21,748

*In December, master commitment conversions exceeded new master & regular commitments taken.

INTEREST RATES AND YIELDS

1- to 4-UNIT MORTGAGES

YEAR AND MONTH	FHA OPINION SURVEY FHA New[4]	FHA OPINION SURVEY CONVENTIONAL New	FHA OPINION SURVEY CONVENTIONAL Existing	FHLBB SURVEY CONVENTIONAL New	FHLBB SURVEY CONVENTIONAL Existing	FNMA 1 Yr. ARM (1%/Yr.)	FNMA FRM Conv.
1987							
FEB	9.86%	9.80%	9.81%	9.12%	9.16%	8.62%	9.64%
MAR	10.28	9.99	10.01	9.15	9.14	8.60	9.74
APR	10.46	10.19	10.19	9.13	9.21	8.86	10.04
MAY	10.84	10.48	10.49	8.95	9.19	9.24	10.28
JUN	10.65	10.35	10.37	9.26	9.28	9.45	10.22
JUL	10.66	10.47	10.47	9.17	9.29	9.67	10.24
AUG$_p$	**n.a.**	**n.a.**	**n.a.**	**n.a.**	**n.a.**	**10.04**	**10.43**

CURRENT SECONDARY MARKET YIELDS

SELECTED SECURITIES

YEAR AND MONTH	GNMA[6]	FNMA[6]	FHLMC[6]	A-Rated[7] Utility	U.S. Government 10-yr.	U.S. Government 26-wk.	Prime Comm. Paper 90-119 Days
1988							
FEB	9.29%	9.27%	9.23%	9.75%	8.21%	5.93%	6.58%
MAR	9.39	9.33	9.29	9.91	8.37	5.91	6.62
APR	9.72	9.62	9.59	10.23	8.72	6.21	6.86
MAY	10.01	10.56	10.25	10.61	9.09	6.53	7.19
JUN	9.97	10.10	10.06	10.41	8.92	6.76	7.49
JUL	9.96	10.35	10.30	10.40	9.06	6.99	7.82
AUG	**10.11**	**10.44**	**10.90**	**10.45**	**9.26**	**7.39**	**8.26**

SPREADS (Basis Points)

YEAR AND MONTH	FHA New Minus A-Utility	GNMA Minus 10-Yr. Govt.	FNMA Minus 10-Yr. Govt.	FHLMC Minus 10-Yr. Govt.
1988				
JAN	12	123	111	101
FEB	11	108	106	102
MAR	37	102	96	92
APR	23	100	90	87
MAY	23	92	147	116
JUN	24	105	118	114
JUL	26	90	129	124
AUG	**n.a.**	**85**	**118**	**164**

NA—Not available. p—Preliminary

[1] From the National Association of Realtors "Existing Home Sales" series

[2] Mutual Savings Banks and Commercial Banks

[3] FHA applications received includes the Direct Endorsement Program starting in 1984

[4] Secondary market gross yields

[5] Federal Home Loan Mortgage Corp. Existing Construction only

[6] Securities for 0 to 30 day delivery

Prior to January 1984 this rate was for Aaa-rated New Issue Utility Bonds

[8] Year-to-date seasonally adjusted series not calculated

[9] 1985 data on mortgage bankers obtained from the HUD Survey of Mortgage Lending Activity